OVERVIEW OF INCOME AND FRANCHISE TAX AND APPORTIONMENT

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Personal Income Tax Calculation

2013 Legislation eliminated many deductions and <u>credits and enacted flat tax rate starting in 2014</u>

- Federal Adjusted Gross Income with Fewer Adjustments
  - Decoupling Provisions from Internal Revenue Code
  - Social Security
  - Retirement Income from Bailey Decision
  - Others

Choose Highest of Two Deductions

Standard Deduction	Real Property Tax, Mortgage Interest, Charitable giving
$15,000 (Joint)	Sum of:
	Mortgage Interest + Real Estate Property Tax capped at $20,000
$12,000 (Head of household)	+
	Charitable Contributions
$7,500 (Single, MFS)	

Child Tax Credit

- $125 per child if AGI =/< $40,000 MFJ
- $100 per child if AGI > $40,000 and < $100,000 MFJ
- No credit if AGI > $100,000 MFJ

Personal Income Tax Rates

2013: Graduated tax rates 6% to 7.75%

<u>2013 Legislation enacted flat tax rate:</u>

2014: 5.8%

2015 and after: 5.75%

Corporate Franchise Tax Calculation

Tax Rate: \$1.50 per \$1,000

Levied on largest of Three Alternate Tax Bases

- Apportioned Capital Base
  - Similarity with net worth calculation, but does not conform to Generally Accepted Accounting Principles
  - Multistate companies apportion the base to NC using apportionment formula used for corporate income tax purposes
- Depreciated value of NC property
- 55% of appraised value of NC property

Corporate Income Tax Rates

2013:	6.9%
2014:	6%
2015:	5%
2016:	4% if FY 14-15 General Fund tax revenues equal or exceed $20.2 billion
2017:	Reduced by 1% if FY 15-16 General Fund tax revenues equal or exceed $20.975 billion

Corporate Income Tax Calculation

- Start with Federal Taxable Income and make adjustments
  - Decoupling Provisions from Internal Revenue Code
  - Interest on U.S. Obligations
  - Deductions taken on income tax paid to other states
  - Charitable contributions
  - Others

Multistate Company Apportionment

- Corporate income and franchise tax is apportioned
- Personal Income Tax is apportioned when there is out of state ownership of S corporations, LLCs, and partnerships
- Required under federal law to prevent the same dollar from being taxed more than once by states

Apportionment Formulas

- Historically, apportionment was intended to be done using a standard, uniform formula among states, based on taxpayer's in-state property, payroll and sales as a percentage of total property, payroll and sales

- As of 2015, only nine states still use the standard formula

- No uniform formula because states have increased the weight of the sales factor or used the sales factor exclusively (Single Sales Factor)

NC Apportionment Formula

- Double Weighted Sales Factor for Most Firms
- Single Sales Factor for Some Firms
  - Qualified Capital Intensive Corporation
  - Excluded Corporations
  - Public Utilities

Comparison of Double Weighted Sales to Single Sales
4% of property and payroll in NC, 2% of sales in NC

Double Weighted Sales Factor	Single Sales Factor
Use the average of four factors: NC share of (Property + payroll + sales + sales)/4 (4% property +4% payroll +2% sales +2% sales)/4 = 3% Apportionment	□ Apportion based only on NC share of sales □ NC property and payroll investment is not considered in determining how much of multistate firm's income and capital is taxed in NC = 2% Apportionment

Apportionment Percentage with $500 million NC investment. NC share of property/payroll increases to 50%

Double Weighted Sales Factor

Use the average of four factors:

NC share of (Property + payroll + sales + sales)/4

(50% property +50% payroll +2% sales +2% sales)/4

=

26% Apportionment

Single Sales Factor

- Apportion based only on NC share of sales
- NC property and payroll investment is not considered in the determining how much of multistate firm's income is taxed in NC

=

2% Apportionment

Tax Liability Comparison: $100 million in Income and $1 billion in Capital before Apportionment

Double Weighted Sales Factor	Single Sales Factor
26% apportionment	2% apportionment
NC taxable income = $26M	NC taxable income = $2M
NC taxable capital = $260M	NC taxable capital=$20M
Income tax = $1,300,000	Income tax = $100,000
Franchise tax = $390,000	Franchise tax = $30,000
Total = $1,690,000	Total = $130,000

Single Sales Factor Policy Considerations

- Economic Development Tool?
  - Tax considerations include not only the tax rate but also what the firm's apportionment percentage will be
  - 21 states now use single sales factor

- Not Everybody wins
  - If % of sales in NC is greater than % of payroll and property in NC, tax liability is higher

Apportionment Formulas
Neighbor States

- South Carolina: Sales factor only
- Georgia: Sales factor only
- Virginia: Double-weighted sales with option of single sales factor apportionment for manufacturing and retail companies
- Tennessee: Double-weighted sales factor

Questions?

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